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FM AMEMBASSY RANGOON
TO RUEHC/SECSTATE WASHDC 7319
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RUEHBJ/AMEMBASSY BEIJING 1791
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UNCLAS SECTION 01 OF 03 RANGOON 000210

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SUBJECT: BURMA - WHY THE KYAT IS APPRECIATING AGAINST THE DOLLAR

REF: A) Rangoon 198 B) Rangoon 137

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11. (SBU) Summary. The Burmese kyat, traditionally one of the weakest currencies in Southeast Asia, continues to appreciate against the declining U.S. dollar. Since September 2007, the market rate of the kyat has risen by 19 percent. Burmese economists see the kyat's appreciation as primarily due to lower demand for dollars, although they acknowledge that the Burmese supply of dollars has increased as businessmen close Singaporean bank accounts and smuggle U.S. dollars into the country. The uncertain political climate surrounding the upcoming May referendum is discouraging companies from doing business in Burma, and the regime is processing business permits even slower than usual, reducing transaction demand for U.S. dollars. Additionally, as the speculative value of the dollar continues to fall, Burmese businesses look to other currencies for financial transactions, further reducing the need for U.S. dollars. While the appreciation of the kyat has resulted in lower inflation, down from 53 percent in September to 29 percent in February, many Burmese find that their purchasing power has not increased. Low salaries and high production and transportation costs continue to push up prices, making it difficult for the majority of Burmese to survive on \$1 a day. End Summary.

Kyat Up, Dollar Down

12. (SBU) Burma is one of the poorest countries in Southeast Asia, ranked 132nd on the UN's 2007 Development Index. Most Burmese earn an average income of \$30/month, and survive on \$1 a day, spending most of their income on food. Since the August 2007 fuel price hike, prices of locally-produced food and commodities, as well as imported goods, have skyrocketed due to higher production and transportation costs. Although Burma's economy continues to

deteriorate due to government mismanagement, we have observed an economic phenomenon that makes little sense given Burma's weak economy: the significant appreciation of the kyat against the U.S. dollar since September 2007.

 Kyat - U.S. Dollar Exchange Rates
 2007-2008*

Month/Year	Average Kyat Rate/\$1	Percent Change**
January 2007	1284	2.23
February 2007	1268	- 1.25
March 2007	1263	- 0.39
April 2007	1265	0.16
May 2007	1263	- 0.16
June 2007	1272	0.71
July 2007	1292	1.57
August 2007	1314	1.70
September 2007	1368	4.11
October 2007	1345	- 1.68
November 2007	1290	- 4.09
December 2007	1280	- 0.78
January 2008	1249	- 2.42
February 2008	1192	- 4.56
March 2008*	1107	- 7.13

 *Through March 14, 2008

**Negative percent change depicts appreciation of the kyat against the U.S. dollar.

13. (SBU) Although the market exchange rate for the kyat against the U.S. dollar has remained fairly constant over the past five years, averaging 1300 kyat/\$1 for the entire year, the kyat has

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appreciated 19 percent against the dollar in the past six months. As of March 14, the market rate of the kyat was 1107 kyat/\$1 compared to 1368 kyat/\$1 in September. While the kyat tends to be stronger vis-a-vis the U.S. dollar during the dry season (November-April) because of the influx of dollars from foreign tourists and relatively high export levels compared to the rest of the year, the kyat only appreciated an average of six percent between September and March during the past three years. This year is the outlier, with no obvious reason why, Kanbawza Bank Consultant U Than Lwin told us.

14. (SBU) The kyat's sudden appreciation surprised Burmese bankers, economists, businessmen, and money traders, who pointed out that the kyat value is more in line with the strong world currencies - the Euro, yen, and Swiss franc - than with regional currencies. It makes sense that the Euro and the yen are appreciating by 12 percent against the dollar, U Than Lwin commented. But that the kyat is outperforming the Singapore dollar or the Thai baht, traditionally stronger regional currencies, defies logic, he stated.

 Foreign Currency Appreciation
 Against the US Dollar
 09/01/2007 - 03/14/2008

Currency	Sept Rate Vs. \$1	March Rate Vs. \$1	Percent Change
Spore Dollar	1.526	1.383	- 9.37
Thai Baht	34.28	31.35	- 8.55
Euro	0.64	0.74	-12.52
Japanese Yen	116.17	100.58	-13.42
Swiss Franc	1.21	1.01	-19.80
Burmese Kyat	1368.00	1107.00	-19.08

 Basic Economics: Supply and Demand

15. (SBU) Why is the kyat appreciating at a substantially higher rate against the dollar in 2007-2008 compared to previous years? While several bankers and money changers told us that it is due to an increased supply of dollars in Burma, local Burmese economist U Myint disagreed, emphasizing that the issue is one of demand rather than supply. According to U Myint, Burma's current political situation and the uncertainty surrounding the upcoming May referendum creates a toxic environment for doing business. Indeed, businessmen have complained to us in recent months that it has become more difficult to secure import and export licenses. Several traders told us that the GOB does not process license requests as quickly as in the past; now it takes up to a month for license approvals. Several garment manufacturers told us that foreign companies are also hesitant to enter into business deals with Burmese companies, afraid that the upcoming referendum could cause instability and undermine business opportunities. Transaction demand for U.S. dollars has declined since September, U Myint declared. While part of the kyat appreciation is due to the cyclical nature of exchange rates, the low demand for U.S. dollars allows the kyat to appreciate further against the dollar.

16. (SBU) Additionally, U Myint noted that the dollar continues to weaken on the world market, further driving down the value locally. In the past, Burmese held on to U.S. dollars for speculative reasons; through arbitrage, they could sell dollars for profit. As the value of the dollar continues to fall, people are less willing to save money by holding U.S. dollars, he stated. Increasingly, businessmen are looking toward alternative currencies, such as the Singapore dollar (ref A), for business transactions and savings,

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relying less on the U.S. dollar. Following the trend of using alternative currencies, business contacts explained that exporters, particularly in the rice sector, have been selling their export letters of credit in advance for kyat, enabling them to purchase products that they will then export. This practice, condoned by the government, further decreases the use of dollars.

17. (SBU) While U Myint emphasized that low demand for dollars was the driving force behind the kyat's recent appreciation, he acknowledged that an increased supply of U.S. dollars played a small role. Dollars are not entering Burma because tourist season (the number of tourists has been down substantially this year) or increased exports, he stated. Instead, many Burmese businessmen, who are having problems with their banks in Singapore, are closing their accounts. If businessmen are unable to open new accounts in Singapore, they withdraw their money in U.S. dollars and smuggle the money into Burma, raising the supply of dollars in the country. Because most Burmese do not declare how much foreign currency they bring into Burma, there is no way to determine how many U.S. dollars are actually in Burma's money supply, U Myint noted.

A Paradox: Lower Inflation, Less Purchasing Power

18. (SBU) Generally, as a currency appreciates, purchasing power also increases, lowering inflationary pressure. In the Burmese case, we have found that only part of the equation rings true. Inflation levels have declined sharply since September, from 53 percent to 29 percent by the end of February. (Note: The Burmese Central Statistical Office has not released inflation data since July 2007. Embassy Rangoon monitors inflation by observing prices of a basket of 37 domestic and imported products. End note.) Prices of goods have remained relatively stable since September, although they have risen somewhat from pre-September levels. Win Win Tint, owner of Burma's largest supermarket City Mart, which predominantly sells imported products, told us that while business has picked up in 2008, the purchasing power of the kyat has not risen as much as it should have. Because salaries have not risen to match inflation, people cannot afford to purchase luxury items, such as imported groceries, and can barely purchase basic foodstuffs. The high costs of production and transportation in Burma translates into high prices of food and commodities, something that will not likely change in the future.

Comment

19. (SBU) Economists are baffled by the kyat's high rate of appreciation in recent months, noting that the rate should be closer to 7 or 8 percent rather than 19 percent. Outside forces, such as the effect of financial sanctions on Burmese bank accounts in Singapore and the government's promotion of the use of Singapore dollars, may further explain why Burma's weak currency has appreciated against the dollar. Despite the higher value of the kyat vis-a-vis the dollar and the lower inflation rate throughout the country, most Burmese continue to struggle to make ends meet. The foreign exchange rate matters little to most Burmese just trying to survive. While the kyat on paper looks strong, the purchasing power of the currency remains low compared to the still-high prices of food and other products in Burma. Until salaries increase to meet inflation or the costs of production and transportation drop, the Burmese kyat will remain a relatively weak currency and the Burmese will continue to spend more than 70 percent of their salary on basic commodities. Only political change will result in leaders willing to seriously correct the dysfunctional Burmese economy.

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